No. 11116

In the United States Circuit Court of Appeals

For the Ninth Circuit

GEORGE M. McBRIDE, Trustee in Bankruptcy of Western Bond and Mortgage Company, an Oregon Corporation, Bankrupt,

Appellant,

vs.

C. H. FARRINGTON,

Appellee.

BRIEF OF APPELLEE

Upon Appeal from the District Court of the United States for the District of Oregon.

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STEVENS-NESS LAW PUB. CO., PORTLAND

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ABSTRACT OF THE CASE

Plaintiff is Trustee in Bankruptcy of Western Bond & Mortgage Company, a corporation, hereinafter referred to as Western Bond and defendant was in 1929 and 1930 a stockholder, director and president of the corporation.

October 2, 1943, plaintiff as Trustee in Bankruptcy, commenced this suit in equity to recover from defendant the value of property alleged to have been fraudulently obtained by defendant from the corporation. The complaint charges two fraudulent transfers. One transfer is alleged to have been made on **December 12, 1929**, involving 40,000 shares of the capital stock of Consolidated Credit Corporation, which stock was owned by the Western Bond. The other is alleged to have been made on **December 20, 1930**, involving the transfer of the capital stock of Western Guaranty Company which was owned by Western Bond.

It is alleged that the transfers were a fraud on creditors and that (Tr. p. 2):

> "The action arises under Section 67 and Section 70 of the United States Bankruptcy Act . . . . ."

November 25, 1931, a Petition in Bankruptcy was filed against the Western Bond. (Tr. p. 27).

August 13, 1934, plaintiff was appointed Receiver in the bankruptcy proceeding. (Tr. p. 27).

December 4, 1934, plaintiff was appointed Trustee. (Tr. p. 27).

To avoid the bar of the Statute of Limitations and Laches plaintiff alleged that he did not discover the fraud until 1943. (Tr. p. 7).

After issue was joined, the court below made an order segregating the issues of limitations and laches from the issues on the merits and directed that they be first tried and determined. (Tr. p. 7).

The suit was tried on the issues of limitations and laches. Judge Fee rendered a written decision in favor of defendant (Tr. pp. 60 to 72) in which he held **upon the facts** and upon the law (a) that the case was governed by the Oregon Statute of Limitations which fixes a period of two years from the discovery of fraud for the commencement of an action; (b) that plaintiff could have discovered the alleged fraud by the exercise of reasonable diligence more than two years prior to the commencement of the suit and was therefore barred by the Oregon Statute of Limitation and (c) that the long delay in challenging the transactions resulted in prejudice to defendant because in the interim participants in the challenged transactions and witnesses having knowledge of material facts had died, that defendant **"had been robbed of a means of defense"** (Tr. p. 71), and that plaintiff was guilty of laches which barred recovery.

The opinion was handed down after an extended colloquy between Judge Fee and counsel for plaintiff-appellant (Tr. p. 278 to 303) in which the court sought to have plaintiff clarify his theory of the case.

The court then made Findings of Fact and Conclusions of Law upon the issues of limitations and laches (Tr. p. 72 to 74).

With respect to discovery of the fraud, the Findings of Fact recite (Tr. p. 73),

> "Plaintiff was appointed trustee in bankruptcy of Western Bond and Mortgage Co. on

December 12, 1934, and all of the records of said corporation were promptly placed in his hands, including a litigation record pointing to the transactions on which plaintiff bases his claims against defendant.

"Prior to 1936 plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge of the matters alleged in the complaint.

"Plaintiff failed to pursue with reasonable diligence the information which had come into his possession prior to 1936 and which pointed to the transactions referred to in the complaint."

With respect to laches, the Findings of Fact set forth (Tr. p. 74),

"Prior to the bringing of this action participants in the transactions referred to in the complaint and others who had known the material facts had died and defendant was deprived of a means of defense through their evidence."

This **Finding of Fact is not challenged by any proper specification of error.**

The Conclusions of Law recite that the action is barred by the provisions of the Oregon Statute of Limitations; that the action is barred by plaintiff's laches and that defendant is entitled to judgment of dismissal (Tr. p. 74).

On the said Findings of Fact and Conclusions of Law judgment dismissing the complaint was entered, and plaintiff now appeals from said judgment.

THE QUESTIONS INVOLVED

1. Are the specifications of error (applt's. br. p. 18) sufficient to present any question for consideration of this court?
2. **Re: Laches**—Is there any substantial evidence to support the findings of the fact?
3. **Re: Statute of Limitations**—(a) Is the Oregon Statute of Limitations applicable? (b) Is there any substantial evidence to support the findings of fact?
4. Are the conclusions of law warranted by the findings of fact?

PRELIMINARY STATEMENT

Appellant presents this case as though the issues for determination arise upon a demurrer to the complaint. He adopts the allegations of the complaint and assumes them to be true. The appeal is not from a judgment entered upon an order sustaining a demurrer to the complaint.

The appeal is from a judgment **entered upon findings of fact** and conclusions of law made **after a trial of the issues of fact** and law on the questions of **laches** and **limitations**.

While the court below did not try and determine the issue as to the alleged fraudulent transfers, and this Court is not now called upon to determine that issue, it cannot be assumed in this case that the allega-

tions of the complaint charging the defendant with the fraudulent transfers are true, as in the case of a judgment based upon a demurrer to a complaint. In this case issue was joined as to these allegations. They have not been tried or determined in this case. Neither has there been any adjudication in any other proceeding that Farrington was responsible for any fraudulent transfers. Hence the assumption of fraudulent conduct by Farrington in this case is unwarranted, and should not prejudice the court in considering the **only issues** which were determined and are now before the court, to-wit: laches and limitations.

Although charges of fraud have been hurled against this defendant since 1931 there has never been any adjudication of misconduct on defendant's part in any proceeding and none in the case at bar.

We, therefore, challenge appellant's right to present his case in this court upon the **assumed guilt** of the defendant, contrary to the cardinal rule that **fraud is never presumed.**

I

THE SPECIFICATION OF ERRORS ARE INSUFFICIENT TO PRESENT ANY QUESTION FOR REVIEW UPON THE ISSUE OF LACHES

Rule 20(d) of this Court requires that the Specification of Errors,

> "Shall set out separately and particularly each error intended to be urged."

And **when Findings of Fact are made,**

> "The specification shall state as particularly as may be wherein the Findings of Fact and Conclusions of Law are alleged to be erroneous."

Findings of Fact on the issue of laches were made in this case.

The Specification of Errors directed to this issue in appellant's brief is as follows: (P. 19)

> "The Court erred in holding that the Trustee was guilty of laches."

We submit that the specification is not a compliance with Rule 20(d), as construed by this Court because it does not point out whether,

(a) Appellant intends to challenge the admission or rejection of evidence pertaining to this issue,

(b) Intends to challenge the credibility of the witnesses,

(c) Intends to challenge the sufficiency of the evidence to support the Findings of Fact,

(d) Intends to challenge the sufficiency of the Findings of Fact to support the conclusions of law that the suit is barred by laches.

Appellant's specification "lumps the entire case", and throws it into the lap of the court.

In **American Surety Co. v. Fischer Warehouse Co., 88 Fed. (2d) 536-539 (9th Cir.) (1937),** this Court said:

> "It is not sufficient that appellant assert generally that the trial court made wrong findings and reached wrong conclusions and then and thereby **invite this court to retry the cause** without indicating to us in such assignments in what respect or for what reason the findings or conclusions are claimed to be in error."

In considering the sufficiency of the assignment of errors in that case, this Court propounded the following inquiry:

> "What was the erroneous basis used, or the erroneous step made by the court which shows his conclusion was wrong? The court might have erred in reaching his conclusion by considering testimony erroneously admitted; by erroneously excluding evidence; by finding a fact not supported by substantial evidence; by the erroneous application of law; or by some other erroneous action. But we consider alleged errors, and if none are assigned, there are none to consider."

In **United States v. Bollman, 81 Fed. (2d) 1009, 9th Cir.,** the Court below made Findings of Fact on which the judgment appealed from was entered. The Court

held that where "findings are not complained of" all errors "based on the trial court's findings are therefore **decreed abandoned.**"

In **Krause v. Snyder,** 87 Fed. (2d) 723-725 (8th Cir.) (1937), the court held:

> "The party complaining of the action of the lower court '**must lay his finger upon the point of objection** and must stand or fall upon the case he made in the court below'."

In **Cohen v. United States, 142 Fed. (2d) 861, 8th Cir.** (1944), the Court held:

> "(1) As has been observed, the action was tried to the court without a jury. No questions are raised as to the admissibility of evidence, nor is there any specific challenge to any ruling of the court, **nor are the findings of the court challenged as not being sustained by the evidence.** . . . . . .
>
> . . . . . .
>
> "In E. R. Squibb v. Mallinckrodt Chemical Works, Judge Stone, speaking for this court . . . said (69 F. (2d) 687):
>
> ' . . . . In short, the appellant has **lumped into this assignment the entire case,** except objections to evidence and no such objections are urged here or preserved in any assignment. All that this assignment amounts to is that a wrong decree was entered. It is a clear violation of rule 11 requiring that assignment of errors shall 'set out separately and particularly each error asserted and intended to be urged' . . . .
>
> " 'Since the specifications and assignments of error present nothing for our consideration, the decree must be and is affirmed.'

> 'In the instant case the questions propounded in the brief challenge no particular action or ruling of the court but at most **question 'the entire case.'** If they be construed as an attempt to question the court's findings as not being sustained by the evidence, it is clear that they do not point out where in or in what particular the evidence is lacking to sustain the findings."

In the case at bar, appellant has "lumped" into the specification the "entire case", insofar as it relates to the issue of laches. The court is invited "to retry the cause" without indicating in what respect the court erred and without challenging the findings of fact.

Under the foregoing decisions the specification of errors with respect to the issue of laches, is insufficient to raise any question for determination by this court. The decision of the court below on this issue should therefore be affirmed.

If appellee is correct in this contention the judgment appealed from must be affirmed because the remaining issue as to the application of the statute of limitations then becomes academic.

II

SCOPE OF REVIEW IN THIS COURT

The issues of laches and limitations were **tried upon the facts.** Findings of Fact and Conclusions of Law were made thereon adverse to the allegations of the complaint.

Rule 52 of the Rules of Civil Procedure provides that:

> "Findings of Fact shall not be set aside unless **clearly erroneous."**

It is the established rule of this Court, as it is in all of the circuits, that a finding is not **"clearly erroneous"** if there is **"any substantial evidence"** to sustain it.

Assuming without admitting that the Specification of Errors properly present the issues, the scope of review in this Court is limited to the ascertainment of the existence of "any substantial evidence" to support the Findings of Fact. It is not even suggested anywhere in the specifications that the Conclusions of Law are not supported by the Findings of Fact.

In **Rogers v. Union Pacific R.R. Co., 145 Fed. (2d) 119, (9th Cir.),** this court said that when a Finding of Fact is supported by substantial evidence, **"we must accept it as correct."**

In **Lumbermens Mutual Casualty Co.** v. **McIver, 110 Fed. (2d) 323 (9th Cir.) 1940,** this court adopted the rule announced by the Supreme Court of the United States in **State Farm Insurance Co. v. Coughran, 303 U. S., 485-58, Sup. Ct. 670,** as follows:

"Under applicable statutes and repeated rulings here, the matter open for consideration upon the appeal was whether the findings of the trial court supported its judgment. **To review the evidence was beyond the competency of the Court."** (citing authority.)

In **Gaytime Frock Co. v. Liberty Mutual Insurance Co., 148 Fed. (2d) 694, 7th Cir., 1945,** the court held:

"Moreover, it is clear from what we have said that the sole question here involved, revolves about the propriety of the **inferences** and conclusions **drawn from the evidence by the trial judge, who had the primary function of finding the facts and choosing from among conflicting factual inferences those which he considered most reasonable.** Under such circumstance our **power is limited to a determination of whether those inferences and conclusions have any substantial basis in the evidence. If such a basis is present the process of judicial review is at an end, ... And even where there is no dispute about the facts, if different reasonable inferences may fairly be drawn from the evidence, we are forbidden to disturb the findings** based on such inferences unless they are clearly erroneous."

In **Scroggs v. American Stove Co., 142 Fed. (2d) 297, 7th Cir. 1944,** the court held:

"Our function is limited to ascertaining if there is any such evidence, and in doing so we must **consider the record in the light most favorable to the plaintiff."**

(All emphasis in quotations supplied by counsel for appellee.)

It must be remembered in this case that the plaintiff had the burden of proof upon the two issues here

involved. The issues were decided against the plaintiff, and so in this case, in order to establish error, he must demonstrate that there is no substantial evidence to support the Findings of Fact, and that he has himself sustained his case by preponderance of the evidence.

Columbian National Life Insurance Co. v. Goldberg, 138 Fed. (2d), 192, (6 Cir.).

We submit that an examination of the record will disclose not only **some** substantial evidence to support the findings of fact, but that no other conclusion was possible.

III

APPELLANT'S CAUSE OF SUIT IS BARRED BY LACHES. THE FINDING OF FACT IS SUPPORTED BY SUBSTANTIAL EVIDENCE.

SUMMARY

I.

Appellant's brief in dealing with the subject of laches (p. 35-36) does not assert or attempt to demonstrate that there is no substantial evidence to support the findings of fact.

II.

Appellent's contention that if the cause of action is not barred by the statute of limitations, it would not be barred by laches, is erroneous as a matter of law.

III.

The application of the doctrine of laches does not merely depend upon the reasons for plaintiff's delay. The doctrine of laches concerns itself with the effect of the delay upon the ability of the defendant to defend himself against the charges and whether he was adversely affected by reason of changed conditions.

IV.

The death of participants in and witnesses to the transaction out of which the litigation arises, the loss of evidence, the dulling of the memory of the surviving parties or witnesses which subject defendant to the hazard that he may not be able to adequately present his defense, makes applicable the doctrine of laches.

V.

The record establishes and the court below made findings of fact that the defendant **would be prejudiced** in this case in the presentation of his defense by reason of the loss of evidence from the death of participants and witnesses. This finding is not challenged.

VI.

Appellant was guilty of gross negligence and failed to exercise reasonable diligence in asserting the claims.

ARGUMENT

It is highly significant that appellant does not in his brief make the slightest attempt to demonstrate that the court below committed error in making the finding of fact that defendant was prejudiced by the delay due to the loss of witnesses through death.

The sole contention on the subject of laches is embraced in appellant's statement (br. p. 35):

> "If the action is barred, laches become an academic question. If the action is not barred laches do not bar it . . . . ."

The first sentence is obviously true. If the action is barred by the statute of limitations it is a complete defense and it is immaterial whether the action is also barred by laches.

But the second sentence which involves the converse is not true. It is settled beyond question that the doctrine of laches applies even though the action is not barred by the statute of limitations.

In **19 Am. Jur. 345**, the text says:

> "On the other hand, where an equitable remedy is sought, the court may refuse its aid although the period which has elapsed without suit is less than that which is prescribed by the statute."

In **Wilson v. Wilson,** 41 Ore. 459-463, the Supreme Court of Oregon held that the laches will bar relief

> **"although the full time may not have elapsed which would be required to bar a remedy at law."**

In **Sedlak v. Sedlak, 14 Ore. 540,** the only case cited by appellant, the Oregon Supreme Court in considering the application of the doctrine of laches said:

> "Sometimes the analogy of the statute of limitations is implied; sometimes a longer period than that prescribed by the statute is required; **in some cases a shorter period is sufficient."**

The decisions of the Supreme Court of the United States, are to the same effect.

> **Alsop v. Riker, 155 U.S. 448-15 Sup. Ct. 162.**
> **Whitney v. Fox, 166 U.S. 637-17, Sup. Ct. 713.**
> **Patterson v. Hewitt, 195 U.S. 309-25, Sup. Ct. 35.**
>
> (All empsasis in quotations supplied.)

The court below decided the question of laches upon the facts. It made the specific finding of fact that:

> "Prior to the bringing of this action, participants in the transactions referred to in the complaint and others who had known the material facts, had died, and defendant was deprived of his means of defense through the evidence." (Tr. p. 74).

In his opinion, Judge Fee pointed out (Tr. p. 70-71) that the transactions were consumated in 1929, ap-

proximately fifteen years ago; that the petition in bankruptcy was filed in 1931; that extensive investigations were made at that time; that the **main actors in the transaction,** with the exception of defendant, **are now dead, as well as others who have known material facts** and **that there is "a detriment to the defendant in that he has been robbed of his means of defense by the death of witnesses and participants."** The suit was commenced in 1943 (Tr. p. 12).

The specification of errors does not challenge this finding of fact, nor is it argued in the brief that there is no substantial evidence to support this finding of fact.

It has been held that **"laches is a question of fact"**, and that "an appellate court will not interfere with its (trial court) discretion in this respect, unless manifest injustice has been done, or unless its conclusion cannot reasonably be held to find support in the evidence."

Wolpert v. Gripton, 2 Pac. 2d, 767 Cal.

Before demonstrating that there is substantial evidence to support the finding of fact, we call attention to the cardinal principles that govern the application of the doctrine of laches.

In **Wood v. Davin, 122 Ore. 74-81,** the Oregon Supreme Court adopted the principles enunciated by the Supreme Court of the United States in **Hammond v. Hopkins,** 143 U.S. 283, in which Chief Justice Fuller said:

> "No rule of law is better settled than that a court of equity will not aid a party whose applica-

tion is destitute of conscience, good faith and reasonable diligence, but will **discourage stale demands** for the peace of society by refusing to interfere where there has been gross laches in prosecuting rights, or where long acquiescence in the assertion of adverse rights has occurred. The rule is particularly applicable where the **difficulty of doing entire justice** arises **through the death of the principal participants in the transaction complained of, or of the witness or witnesses,** or by reason of the original transactions having become so obscured by time as to render the ascertainment of the exact facts impossible."

In **Wilson v. Wilson, 41 Ore. 459-463,** the Oregon Supreme Court held:

"If by the laches and delay of the complainant it has become **doubtful** whether adverse parties can command the evidence necessary to a fair presentation of the case on their part, ... a court of equity will not interfere to give relief, but will remain passive."

In **Penn. Mutual Life Insurance Co. v. Austin, 168 U.S. 685,** the Supreme Court said:

"It is well established that if by laches and delay of the complainant, it has **become doubtful whether adverse parties can command the evidence necessary** to a fair presentation of the case on their part, as for instance, **where parties interested and witnesses have died in the interim,** . . . . . a court of equity will not interfere to give relief but will remain passive."

In **21 C.J. 226, Sec. 222,** the writer says:

"**Evidentiary Effect of Delay.** Long lapse of time, if unexplained, may create or justify . . . . . . a presumption that the evidence

of the transaction in issue has been lost or become obscured, or that conditions have changed since the right accrued, and that in consequence the adverse party, would be prejudiced by its enforcement."

In 21 C.J. 236, the writer says:

"To bring the rule into operation, it is not necessary that the court should be convinced that the original claim was unjust or has been satisfied; it is sufficient if the court believes that under the circumstances it is too late to ascertain the merits of the controversy. . . . . In any event, loss or obscuration of evidence is a material circumstance to be considered in determining whether the asserted claim shall be enforced; it creates or justifies a presumption against the existence or the validity of plaintiff's right and in favor of the adverse right of defendant."

In **Sheehan v. Municipal Light & Power Company, 54 Fed. Supp.** 169-173, affirmed **151 Fed. 2nd** 65, the court held:

"The testimony of Leach and Lasher and of officers of Edison Company, its general counsel, its attorney and many others who participated in the transactions who are now dead, is now unavailable. Minnie Sheehan accordingly was guilty of laches prejudicial to the defendants." (citing many cases.)

We submit that in the case at bar there is ample evidence to support the findings of fact of the court below on the question of laches, and that the facts found by the court below brings the case within the principles set forth in the foregoing authorities.

To fully appreciate the effect of the 15-year delay it is necessary to briefly outline the nature of the transactions out of which this suit arises. The two challenged transactions took place in 1929 and 1930, respectively. The suit commenced in 1943 and tried in 1944.

The essence of the charge with respect to the 1930 transaction is that defendant-appellee entered into a scheme with one Edward F. O'Flynn, who was president and in control of a corporation called the Massachusetts Mortgage Company, by which defendant caused the Western Bond and Mortgage Company to transfer to him or corporations controlled by him, assets owned by the bankrupt corporation, to-wit, a block of Western Guaranty Stock valued in excess of $300,000 in exchange for certain assets which defendant simultaneously was to receive from O'Flynn, or the Massachusetts Mortgage Company, which had no value. The alleged valueless assets are as follows:

(a) 100 shares of capital stock of Lake Lucerne Co.

(b) Conditional Sales Contracts of automobiles.

(c) Chattel mortgage on personal property.

(d) Promissory note made by Birwell and indorsed by Massachusetts Mortgage Co.

(e) Note of Massachusetts Mortgage Co.

The alleged vice in the transaction is summed up by plaintiff's witness, Erickson, to the worthlessness of the assets received by Western Bond as considera-

tion for the transfer of the Western Guaranty stock (Tr. p. 160-164).

Edward F. O'Flynn, who was the principle participant, in the transaction, died long prior to the commencement of this suit (Tr. p. 137).

The defendant was represented in that transaction by Arthur C. Spencer, an attorney. He died prior to the commencement of this suit (Tr. p. 197).

Judge Carey was Corporation Commissioner of the State of Oregon. Investigation into the affairs of the bankrupt corporation, including the transfer of its assets, were carried on by authority of his department. He died long prior to the commencement of this suit (Tr. p. 198).

Plaintiff claims that he was prevented from carrying on investigation by Hon. A. M. Cannon, referee in bankruptcy, in charge of the bankrupt estate on the alleged ground that it did not seem likely that the estate would have assets (Tr. p. 91-92). The referee in bankruptcy died long before the commencement of this suit and was not available to admit or deny the plaintiff's excuse for the failure to carry on the investigation.

All persons participating in the transfers by and to the bankrupt corporation, are charged with bad faith, with causing misleading and false entries to be made in the books and that the transactions were hidden and disguised by the organization of dummy corporations (Tr. p. 7).

In order to determine the charges thus made, the good faith of the transactions, the honesty of purpose, the regularity of the transactions, the reasons which motivated the transactions and the purposes sought to be obtained, it would be necessary to bring before the court the actors who participated in the transactions and the witnesses who had opportunity to observe and know what was taking place. It would be necessary to establish the entire background and setting in which the transactions took place.

It is obvious that the death of Edward F. O'Flynn and of Mr. Arthur E. Spencer precludes any fair presentation of the history and the facts pertaining to the transaction. They were the principal participants therein. They alone could bring before the court all those details from which the court could determine the good faith of the transaction.

The death of the referee in bankruptcy made it impossible to challenge the truth of the trustee's testimony by which he attempts to throw the blame for his inaction upon the referee in bankruptcy. We believe that if the referee in bankruptcy was alive he would have denied the story that he discouraged investigation of the matters under consideration. But he is not here and defendant is deprived of the opportunity to test the truth of that story. It is not likely that the Referee would sanction failure to perform the mandatory duties imposed on the trustee by Sec. 47a-7 and 8 of the Bankruptcy Act.

The record discloses that difficulties were encountered from the loss of records and efforts to locate them were fruitless.

It is obvious too that the defendant would be at a tremendous disadvantage and subject to a great hazard in any attempt to disprove the allegation that the assets received by the bankrupt corporation were without value.

Fifteen years after the transaction we would be called upon to investigate the financial condition of the Lake Lucerne Company to ascertain the book value or intrinsic value or market value of 100 shares of its capital stock. This would involve the ascertaining (as of 1929-1930) of all of the assets and liabilities of that corporation, the value of its assets, the nature of its business, whether its operations were profitable, and a multitude of elements and details which are necessarily involved in determining the value of the capital stock of a corporation **which is not listed on a stock exchange.**

Fifteen years after the transaction we would be called upon to investigate the value of a block of automobile conditional sales contracts. This would involve an intimate knowledge (as of 1929-1930) of the particular automobiles, the makes, the age, the physical condition, the relation between the value of each automobile and the balance owing thereon, the financial responsibility of the purchaser and a multitude of other facts which is inherent in any inquiry as to the value of any conditional sales contracts, including expert testimony as to the market value of the auto-

mobiles themselves **as of that time.**

Fifteen years after the transaction we would be called upon to investigate the value of the chattel mortgage upon the personal property. This would, of course, require evidence of the kind and character of the personal property, its physical condition, the market value of the property at that time, as well as investigation as to the responsibility of the maker of the note and mortgage at the time of transfer.

Fifteen years after the transaction we would be called upon to investigate and determine the value of the Birwell note, which was indorsed by the Massachusetts Mortgage Company. This would involve an investigation of the financial responsibility of the maker of the note, knowledge of his assets and liabilities as of that time and the investigation into the financial responsibility of the Massachusetts Mortgage Company, the indorser on said note which would, of course, involve investigation of the assets and liabilities of that company and the multitude of details which is inherently involved in such an investigation.

We believe that the court could take judicial notice of the difficulties which would now present themselves in a trial of the issues of the value of those assets at that time. It is obvious that defendant would be greatly prejudiced if **now** called upon to meet that issue.

The burden was on the plaintiff to plead and prove facts which would prevent the bar of laches

from applying to this case. Plaintiff recognized and assumed that burden. To that end he made allegations in his complaint to excuse laches and introduce evidence for the purpose. It was incumbent upon plaintiff to show affirmatively by clear and convincing evidence that the defendant would not be prejudiced by the delay. This he could only do by the introduction of evidence that the means by which all of these questions could be fairly tried and justly determined, were available. Instead, plaintiff's own case demonstrated the inability to produce important evidence, important witnesses, lack of essential records, and the dullness of memory of those who purported to give some information upon that matter involved.

It is not only "doubtful" whether defendant can command the evidence necessary to a fair presentation of the case on his part, **(Penn. Mutual Life Case, 168 U.S. 683)**, but it is well nigh impossible to do so. As it was said in **Smith v. Thompson, 54 Am. Dec. 126-129 Va.:**

> "There can no longer be a safe determination of the controversy and their (plaintiff's) adversaries are exposed to the danger of injustice from the loss of information and evidence."

Under similar circumstances the court in **Hawley v. Von Lanken, 106 N.W. 436,** said:

> "Any conclusion the court may arrive at must at best be conjectural. . . . . ."

It is not necessary in order for the bar of laches to be applied that it should appear to a certainty

that the defendant would be prejudiced by the lapse of time. It is sufficient if it is "doubtful" whether he can fairly present his defense and that it is "too late" to ascertain the merits of the controversy. (21 C.J. 236.)

The 1929 transaction involved the transfer of 40,000 shares of capital stock of Consolidated Credit Corporation, which was owned by the Western Bond and Mortgage Company, in exchange for all of the capital stock of the Keystone Finance Company (Tr. p. 6). The vice claimed in that transaction is that the Western Bond was already the "beneficial owner" of the Keystone Stock and therefore, received nothing of value for the transfer of the Consolidated stock.

Plaintiff attempted to develop the "beneficial ownership" of the Keystone stock through a rather involved process.

Erickson, the accountant, testified (Tr. p. 148) that he found from the minute book of the Keystone Company that the stock of that company when organized was paid for by the transfer to it of 8920 acres of land, which was known as the Keystone Ranch. This conveyance to the Keystone Company in payment of the original subscription to its stock was made by two individuals, Tapfer and Snodgrass (Tr. p. 169). The witness, Erickson, pointed out, however, that in 1925, that ranch stood in the name of Russell Land and Livestock Company, which was a wholly owned subsidiary of Western Bond (Tr. p. 148) and it is therefore asserted that the parties who purported to convey the ranch to the Keystone Corp. for

its stock, had no title, that the title was actually in the Russell Land and Livestock Company since 1925, which was a subsidiary of the Western Bond, and therefore, Western Bond was the owner of the ranch through the medium of the Russell Land and Livestock Company.

Erickson testified that the abstract of title showed that **prior to** 1925 the ranch was owned by a man named Russell, that he transferred it to the corporation, Russell Land and Livestock Company **in 1925** and **in 1929,** Russell Land and Livestock Company, transferred the property to the Keystone Finance Company, but Tapfer and Snodgrass are not shown as being at any time as owners of the land (Tr. p. 169). This is the trustee's contention with respect to that item.

Now, it is apparent that the determination of that issue depends upon whether Tapfer and Snodgrass were the legal or equitable owners of the ranch, or Russell Land and Livestock Company was the owner.

It must be remembered that Erickson only testified to what an abstract of title purported to show. But this does not preclude the fact that Tapfer and Snodgrass may have been the legal or equitable owners of the ranch at the time it was conveyed to the Keystone Finance Company. In may be that it was bought with their money and that they had the equitable estate. An abstract of title does not determine ownership. It merely purports to show what the records of a county clerk's office discloses. But all titles are not determined by recorded instru-

ments. Frequently they depend upon inheritance, through descent, and distribution or by will. They may be evidenced by unrecorded conveyances which are valid as between the immediate parties and other facts which give rise to equitable estates.

To compel defendant to try the issue of **title in Tapfer and Snodgrass** subjects him to the type of hazards recognized by the authorities which we have cited. There is **no evidence whether Tapfer and Snodgrass were available** so that the facts pertaining to their interest in the land could be ascertained. In view of the fact that plaintiff has the burden of proof, it was incumbent upon him to show that Tapfer and Snodgrass were available and the means by which the true ownership of that title, **legal as well as equitable**, can not be determined with the degree of certainty which a judicial determination contemplates.

The difficulty in meeting that issue, due to the lapse of time, warrants the application of the bar of laches.

Re: Lack of Diligence

Appellant presents the question of laches as though it were conceded or the court had found as a fact that appellant had exercised reasonable diligence in ascertaining the facts, and in the commencement of the suit. He cites the **Sedlak case** (appellant's brief, p. 35), which recognizes the rule that lapse of time will not bar a remedy if the plaintiff was ignorant of the fraud. But the very excerpt which the

appellant cites says that ignorance **must not be due to negligence** and that

> "if by reasonable diligence the fraud could have been discovered or ought to have been known, he will be deemed guilty of laches or acquiescence and equity will refuse to interefere."

In the case at bar, the court made findings of fact contrary to the assumed fact upon which appellant proceeds.

The findings set forth (Tr. p. 73):

> "Prior to 1936 plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge of the matters alleged in the complaint.
>
> "Plaintiff **failed to pursue with reasonable diligence the information which had come into his possession prior to 1936 and which pointed to the transactions referred to in the complaint."**

The very foundation for appellant's contention is thereby removed and he is brought within the rule which precludes relief to the plaintiff.

The only way appellant could escape the effect of these findings is to demonstrate that there is not "any substantial evidence" to sustain those findings and that they are "clearly erroneous", and that, appellant has not done.

IV

THE OREGON STATUTE OF LIMITATIONS APPLIES TO THE CASE AT BAR. IT IS NOT GOVERNED BY SECTION 11(d) OF THE BANKRUPTCY ACT (11 U.S.C.A., 29(d)), BECAUSE THE CAUSE OF ACTION PROSECUTED BY THE TRUSTEE IS AN INHERITED ONE.

ARGUMENT

The court below held that the cause of action set forth in the Complaint was not created by the Bankruptcy Act; that the cause of action was in existence prior to and independent of the bankruptcy proceeding and was inherited by the trustee; that it was governed by the Oregon Statute of Limitations (Opinion of Judge Fee, Tr. p. 62 to 66).

Appellant has abandoned specification of error No. 1 which says that "the court erred in determining that the Oregon Statute was applicable," because the contention is not argued in the Brief. Appellant in effect concedes that in this jurisdiction, the law is that the State Statute applies as contended for by Appellee and as decided by the court below.

Appellant's counsel, after conceding that this court will probably so hold (Br. p. 23), states:

> "We do not waive the point, but we shall not further discuss it (Appellant's Brief, p. 23)."

It is the general rule that a specification of error which is not argued will be deemed abandoned and will not be considered by the court.

O'Brien's Manual of Fed. App. Pr., 3rd Ed., p. 212.
McCarthy v. Ruddock, 43 Fed. (2d) 976 (9th Cir.).
Forno v. Coyle, 75 Fed. (2d) 692 (9th Cir.).
Humphreys Gold Corp. v. Lewis, 90 Fed. (2d) 896 (9th Cir.).
Schroepfer v. Abell Co., 138 Fed. (2d) 111-116 (4th Cir.).

In any event we believe there is no escape from the conclusion reached by Judge Fee upon this phase of the case (See opinion, Tr. p. 62-66 and authorities there cited).

Section 1-201, Oregon Compiled Laws Annotated, provides:

> "Actions at law shall only be commenced within the periods prescribed in this title after the cause of action shall have accrued; . . . . ."

Section 1-206 provides:

> "Within two years . . . . an action for . . . . any injury to the person or rights of another not arising on contract . . . . provided that in an action at law based upon fraud or deceit, the limitation shall be deemed to commence only from the discovery of the fraud or deceit."

Section 9-103, Oregon Compiled Laws Annotated, makes the foregoing statutes ~~and~~ of limitations applicable to suits in equity.

Judge Fee predicated his decision upon the ruling of this court in **Davis v. Willey, 275 Fed. 397, 9th Cir.,** which affirmed the decision of the District Court, 263 **Fed.** 588.

In a later case, **Meikle v. Drain, 69 Fed. 2nd, 290, (9th Cir.)**, this court adhered to the ruling made in **Davis v. Willey**. It is interesting to note that Mr. Teiser, counsel for appellant in this case, was one of the attorneys in the Meikle case and it was there urged, in his Brief, that the ruling of this court in the **Davis case** was erroneous and should be overruled. This court declined to do so and reiterated its ruling in the **Davis** case. Because of these decisions, appellant's counsel now makes the admission that "this court would probably hold that the State Statute would still apply." (Br., p. 23).

In **Nairn v. McCarthy, 120 Fed. 2nd, 910**, the Circuit Court of Appeals for the 7th Circuit, followed the **Davis and Meikle** cases and went a step further. It held that Section 11(d) of the Bankruptcy Act (prior to Chandler Amendment):

> "Does not grant an extension of time, but is a prohibition against the institution of actions either by or against the trustee subsequent to the designated time."

The court went on to say:

> "It does not follow from the fact that the trustee is prohibited from bringing an action subsequent to that time that he is authorized to maintain an action prior thereto, irrespective of an applicable limitation statute. The provision is more for the protection of the trustee than for his benefit and, in any event, is for the purpose of terminating his duties and responsibilities . . . **We are of the opinion that the State Statute of Limitation controlled . . . .**"

On p. 23 of Appellant's Brief, the **Narin case** is erroneously listed as being opposed to the **Davis & Meikle cases.**

In **Herget v. Central National Bank & Trust Co., 324 U.S. 4-65, Sup. Ct. 505,** the Supreme Court places the **Nairn case** in the group that supports the proposition that the State Statutes of Limitations applies to inherited causes of action.

The decision in **Harrigan v. Bergdoll, 270 U.S. 560-46, Sup. Ct. 413,** supports the ruling of this court in the **Davis** and **Meikle** cases. The court said:

> "The Bankruptcy law . . . . . does not modify this right of action against the stockholder or create a new one, it merely provides that the right created by the State law shall pass to the trustee and be enforced by him for the benefit of creditors."

The decision of this court also finds support in **Charlesworth v. Hipsch, Inc., 84 Fed. (2d) 834-837 (8th Cir.).** The court there said:

> ". . . . time in which the trustee may sue can not be extended by a provision in the Bankruptcy Act which purports only to limit the time within which a suit may be brought by or against him. . . . . ." (citing several cases).

In **Bovay v. Byllbsby, 12 Atl. (2) 178 (Del.),** the court held that an action by a trustee in bankruptcy to recover from officers and directors of a corporation monies fraudulently obtained, is **"of a dirivative nature".**

V

THERE IS ABUNDANT SUBSTANTIAL EVIDENCE TO SUSTAIN THE FINDINGS OF FACT NUMBERED III, IV, AND V, AND THE FINDINGS OF FACT SUSTAIN THE CONCLUSION OF LAW THAT THE ACTION IS BARRED BY THE OREGON STATE OF LIMITATIONS.

ARGUMENT

The alleged fraudulent transfer of the Consolidated Credit Corporation stock took place **December 12, 1929** (Tr. p. 6) and the Western Guaranty stock **December 20, 1930,** (Tr. p. 3).

Petition in Bankruptcy was filed November 25, 1931, (Tr. p. 2). Plaintiff was appointed Receiver August 13, 1934 and was appointed Trustee December 4, 1934 (Tr. p. 3). This action was commenced October 2, 1943 (Tr. p. 12).

The court below made findings of fact and conclusions of law on the issue of the statute of limitations (Tr. p. 73-74) quoted at page 4 of this brief.

The sole question is now whether there is **"any substantial evidence"** to sustain those findings of fact.

General Principles Governing the Question as to What Constitutes Discovery of Fraud.

Under **Sections 1-201 and 1-206,** made applicable to suits in equity by **Section 9-103, Oregon Compiled Laws Annotated,** already quoted on page 31 of this brief, the statute of limitations bars an action for fraud two years after the cause of action accrues, and the cause of action accrues at the time of the discovery of the fraud.

In the **Linebaugh v. Portland Mtge. Co., 116 Ore.** 1-8, the Oregon Supreme Court construed the provision as follows:

> "The statutory provision that, 'the limitation shall be deemed to commence only from discovery of the fraud or deceit,' properly interpreted, means from the time the fraud was known or could have been discovered through the exercise of reasonable diligence;
>
> . . . . . .
>
> "As stated in Noyes v. Parsons, et al, supra: 'Whatever is notice enough to **excite attention and put a party upon his guard** or call for an inquiry, is notice of everything to which such inquiry might have led.' "

This principle has never been departed from in Oregon and since the case involves the Oregon statute of limitations, we deem that ruling to be controlling.

The Oregon rule is in harmony with the rule laid down by the **Supreme Court of the United States in the leading case of Wood v. Carpenter, 101 U.S. 135,** and the rule laid down by this court in **Prentiss v. McWhirtier, (9th Cir.) 63 Fed. (2) 712:.**

In **Wood v. Carpenter, supra,** the Supreme Court said:

> "Statutes of limitation are vital to the welfare of society and are favored in the law. They are found and approved in all systems of enlightened jurisprudence. They promote repose by giving security and stability to human affairs. An important public policy lies at their foundation. They stimulate to activity and punish negligence. While time is constantly destroying the evidence of rights, they supply its place by a presumption which renders proof unnecessary. Mere delay, extending to the limit prescribed, is itself a conclusive bar. The bane and antidote go together.
>
> . . . . . .
>
> "Whatever is notice enough to **excite attention and put the party on his guard** and call for inquiry is notice of everything to which such inquiry might have led. **When a person has sufficient information to lead him to a fact, he shall be deemed conversant of it."**
>
> . . . . . .

In **Avery v. Cleary, 132 U.S. 604,** it was held that this rule applies with greater force in bankruptcy proceedings because

> "That object was to secure a **prompt determination of all questions arising in bankruptcy proceedings, and a speedy distribution of the assets of bankrupts among their creditors."**

In **Prentiss v. McWhirtier, supra,** this court said:

> "Under the cases in this state (California) it is not enough to assert that the discovery was not sooner made. It must appear that it could not have been made by the exercise of reasonable diligence; and all that reasonable diligence would have disclosed plaintiff is presumed to have

known, means of knowledge in such a case being the equivalent of the knowledge which it would have produced."

In 37 C.J. 976, the writer says:

"**Ignorance of Details or Evidence**—In General.—It is not necessary that a party should know the details of the evidence by which to establish his cause of action. It is enough that he knows that a cause of action exists in his favor, and when he has this knowledge, it is his own fault if he does not avail himself to those means which the law provides for prosecuting or preserving his claim."

U. S. v. Christopher, 71 Fed. 2nd 764, 10th Cir., the court said:

"Discovery does not mean resort at leisure to known sources of information. Possession of the means of knowledge is tantamout of knowledge itself."

In approaching the appraisal of the evidence it should be borne in mind that a trustee in bankruptcy is a quasi officer of the court (**Zimmerman v. Farmington Shoe Co., 31 Fed. 2nd, 405**). He is charged with the duty of collecting and recovering all property of the bankrupt for liquidation and distribution to creditors. He must exercise due diligence in this respect. If he fails to take proper steps to secure all assets he is presumably negligent and may be charged with the value of the assets lost. (re: Reinboth, 157 Fed. 627).

The Bankruptcy Act imposes upon a trustee in bankruptcy, the duty of making an examination of

the bankrupt. This duty is not imposed upon the trustee only when he has reason to believe frauds have been committed. It is his absolute duty to make an investigation into the affairs of the bankrupt to discover whether any fraudulent transfers were made.

Section 47, Bankruptcy Act—11 U.S.C.A. 75.

Section 21(a) of the Bankruptcy Act—11 U.S.C.A. 44(a), affords the trustee in bankruptcy very effective facilities for the investigation of all of the transactions of the bankrupt. It authorizes the examination of "any" designated persons, including the bankrupt. The scope of the examination under this section of the bankruptcy act is very broad. The widest latitude is permitted. The examination can be "searching" and "summary". The act authorizes examination in order to enable the trustee to ascertain whether there has been "fraudulent disposition" of the property and in connection therewith the production of books, papers and documents will be enforced.

> **(Vol. 5, Remington on Bankruptcy, (4th Ed.) Sections 1997 and 1998,** and cases there cited in support of the text.)

In **Kinder v. Scharff, 231 U.S. 517-34, Sup. Ct. 164,** the court rejected the trustee's contention of lack of knowledge because he did not avail himself of the facilities for examination under **Sec. 21(a)** of the Bankruptcy Act. The Supreme Court affirmed the decision of the Louisiana Supreme Court which held (55 So. 769-711) that the alleged fraud would have been discovered if the examination under Sec. 21(a)

of the Bankruptcy Act had been conducted. The court said:

> " . . . . . A litigant who has voluntarily abstained from availing himself of the means put in his hands by the law itself for the ascertainment of a suspected fact cannot be allowed to plead his ignorance of such fact for arresting the course of the statute of prescription and repose. The law upon that point is fully settled."

The urgency of a thorough investigation in this case was apparent because at the time of his appointment and even before, plaintiff knew that Farrington and others were under a cloud of suspicion that he had caused assets of the corporation to be fraudulently disposed of.

Judge Fee's summary of the pertinent facts in his opinion (Tr. p. 60-62) are clearly established by substantial evidence and sustain the findings of fact that plaintiff had knowledge and the means of knowledge, which if pursued would have disclosed all the pertinent facts pertaining to the transactions described in the complaint.

Even a cursory examination of the bankrupt's books would have disclosed that shortly prior to the filing of the bankruptcy petition, two large transfers of assets had been made (the transfers involved in this case.) One transfer was made less than a year prior to the filing of the petition in bankruptcy and the other less than two years prior thereto. These two transfers totalled in excess of $140,000.00. They were unusual transactions and out of the ordinary course of business and therefore challenged attention

and investigation as a matter of course, particularly so because the entries disclosed that the Consolidated Credit Corporation stock was exchanged for the Keystone stock which was owned by the Western Bond and (Tr. p. 144) the Western Guaranty stock was not transferred for money, but was exchanged for other assets.

Plaintiff was an attorney (Tr. p. 84), and for ten years prior to his appointment as trustee, he was Chief of the Division of the State Tax Department and later Chief of the Income Tax Department of the United States Bureau of Internal Revenue (Tr. p. 97-98). He had considerable knowledge of accounting (Tr. p. 98) and in later years held himself out as an income tax counselor. (Tr. p. 103).

Plaintiff had available the facilities and assistance of (a) the Attorney General of the State of Oregon, (b) the Corporation Department of the State of Oregon, (c) two auditors of the Corporation Department without limit as to the services they were to perform (Tr. p. 190, 193, 194, 195, 196, 197), (d) he was paid a salary of $150.00 a month by the State of Oregon and office facilities and office expense, (e) he had the assistance and advise of Mr. John Latourette, an attorney employed with the approval of the bankruptcy court for about one year, (f) and the assistance and advice of Mr. Teiser, present counsel (one of the ablest bankruptcy attorneys practicing at this bar) employed with the approval of the court, and (g) the services of the certified public accountant, Mr. Erickson, since 1936, who had contracted to render

services on all phases of the bankruptcy proceedings on a contingent basis. All this to aid in the investigation into the transactions which precipitated the bankruptcy and the recovery of assets alleged to have been fraudulently transferred.

Immediately upon his appointment he was made aware of the charges that were being asserted against Farrington and others.

Mr. Moody, Assistant Attorney General, called upon plaintiff immediately after his appointment as receiver (Tr. p. 190) and told him of the prior investigations that had been conducted and impressed upon plaintiff the importance of conducing the investigation. He called his attention to the newspaper accounts (Tr. p. 194) and the litigations in the state and federal courts charging Farrington with fraudulent transfer of assets including the transactions involved in this case. Mr. Moody made available to plaintiff the auditors of the Corporation Department (Tr. p. 193), and arranged for the payment to plaintiff of salary and expense by the State of Oregon (Tr. p. 195). Upon his appointment plaintiff came into possession of the books and records of the bankrupt company and its subsidiaries.

These were the auspices under which plaintiff entered upon the performance of his duties as receiver and trustee.

Transfer of Western Guaranty Stock

To simplify presentation of this matter we will treat Farrington and Laurel Investment Company as a unit and as though the transactions were directly between Farrington and the Western Bond and Mortgage Company.

The vice in the Western Guaranty stock transaction as presented by the complaint and developed by the evidence is:

(a) That Farrington obtained from the Western Bond all of the capital stock of the Western Guaranty Company worth $322,014.35; that Farrington caused to be transferred to the Western Bond as consideration therefor, the following assets:

1. 100 shares of capital stock of Lake Lucerne Company, a Washington corporation, without par value.
2. Conditional sales contract on automobiles with unpaid balances amounting to $22,661.03.
3. Mortgage from Ljungdahl Products Co. to Massachusetts Mortgage Co., recorded in Records of Chattel Mortgage, Pierce County, Wash., amount of unpaid principal $24,750.00.
4. Note, W. I. Birwell to Massachusetts Mortgage Co., dated October 6, 1930, $19,477.70.
5. Note of Massachusetts Mortgage Co. to Laurel Investment Co. dated December 20, 1930, for $87,000.00.

and that said assets were worthless. (Plaintiff's contention, pretrial order, Tr. p. 42).

(b) That Farrington obtained the assets which he transferred to the Western Bond as consideration for the Western Guaranty stock from Edward F. O'Flynn and his associates, or Massachusetts Mortgage Co., simultaneously with or shortly prior to the alleged transfer (Plaintiff's contention, pretrial order, Tr. p. 42-45).

The alleged fraudulent character of the transaction was summarized by plaintiff's witness Erickson, who claims to have discovered the alleged fraud as follows:

> "The material fact is that **simultaneous character of these transactions,** the use of the assets for two purposes simultaneously and the further fact that the assets were shown to have had **no value.**" (Tr. p. 162).

We deem the second contention to be wholly irrelevant, because if the Western Bond received assets of equal or greater value, then it was not damaged and neither the corporation prior to bankruptcy nor its trustee after bankruptcy would have any cause of action. And it is so conceded in the testimony. Erickson testified: **"If they did actually receive assets of value compared to what they parted with, they could not question the transaction."** (Tr. p. 160-161). It is obviously immaterial when or how or from whom defendant obtained the assets which were turned over to Western Bond in consideration for the transfer of the Western Guaranty stock, if said assets

were in fact of equal or greater value.

The only issue therefore, which can properly present itself now, is whether there is any substantial evidence to support the findings of fact that plaintiff had knowledge that the assets received in consideration were valueless or whether he could have by the exercise of reasonable diligence ascertained that fact more than two years prior to the commencement of this action.

The record establishes beyond question that **the transaction was spread upon the records of the corporation contemperaneously with its consumation.** The records of the corporation came into the possession of the plaintiff in the fall of 1934. (Tr. p. 131).

The "agreed facts" in the pretrial order (Tr. p. 21) recite that under date of December 15, 1930, the books of the Western Bond recorded the transaction whereby assets owned by Western Bond were transferred to the Western Guaranty Company, for all of its capital stock and the journal entries recording the transaction are set forth.

The "agreed facts", (pretrial order, Tr. p. 23) also recite that on December 20, 1930, at a special meeting of the directors of Western Bond, presided over by Farrington, O'Flynn and Johnson were elected directors; that the meeting recessed for a half an hour; that it reconvened; that defendant and others resigned as officers and directors; that the board then elected Johnson as president and O'Flynn as secre-

tary-treasurer; that a resolution was adopted (Tr. p. 24), authorizing the transfer to Farrington, (Laurel Investment Co.) all of the capital stock of Western Bond and in exchange therefore, to take an assignment from Laurel Investment Company, of the assets specifically described above which were enumerated and described in the resolution. It was further resolved at that meeting (Tr. p. 24), **that in the judgment of the directors that the assets received by Western Bond in exchange for the stock of Western Guaranty: "are of equal or of greater value, than those so to be assigned to Laurel Investment Co. . . ."**

The agreed facts also recite (Tr. p. 24) that on December 20, 1930, Laurel Investment Company transferred to Western Bond the assets specifically described above and received from Western Bond the stock of Western Guaranty.

Plaintiff testified (Tr. p. 96) that he inspected the main books of the Western Bond.

He knew that Farrington had sold his stock in the Western Bond in 1930 to Mr. O'Flynn, or the Massachusetts Mortgage Company, which he controlled, (Tr. p. 131), and that Farrington had retired as an officer and director after December 20, 1930. He testified, **"I knew it from the corporation's records, yes."** (Tr. p. 131).

Mr. Erickson, the certified public accountant, employed by the plaintiff in 1936, occupied offices in the same suite with Mr. Teiser (Tr. p. 140). He was first

employed by plaintiff in June or July of 1936, (Tr. p. 153).

Erickson testified (Tr. p. 157):

> "Q. In respect to this Western Guaranty transaction, **that whole transaction was set up on the books and in the journal and in the minute book, was it not?**
>
> A. **There is a journal entry recording the disposition by the Western Bond and Mortgage Company of the stock in the Western Guaranty Company, for which they were supposed to have received certain assets, and there is a recital of the transaction in the minute book.**"

He testified that the minute book shows that Farrington went out of the management and directorate and that O'Flynn and his associates came in (Tr. p. 158), and that the minute book shows that there was a meeting on December 20, 1930, when Farrington and McCroskey resigned and O'Flynn and someone else took his place; that there was an adjournment of 30 minutes and upon resumption of the meeting, the minutes "set forth the trade of the Western Guaranty stock for those other items which were supposed to have been received." (Tr. p. 159).

He testified that the transaction is referred to at a later place in the minutes, some **two weeks later,** which shows there was a stockholders meeting at which the **transaction was ratified.** (Tr. p. 159-160). He testified:

> "Q. So that the transaction was there for anybody to examine that wanted to?
>
> A. What is recited there is easily read, yes."

He did not make any appraisal of the assets the Western Bond received in the transaction. (Tr. p. 160).

He was asked what it was that he discovered in the books in addition to what is in them now in respect to this Western Bond transaction, (Tr. p. 161), and he answered:

> "The material fact is the simultaneous character of these transactions, the use of the assets for two purposes simultaneously and the further fact that the assets were shown to have had no value."

The then testified that he discovered that the transactions were simultaneous in the Revenue Agent's report (Tr. p. 162).

At (Tr. p. 164) the testimony is as follows:

> "Q. Well, what you have discovered, then, was that the transaction, you claim, was simultaneous instead of an interval having elapsed, and that Farrington and Laurel Investment Company had acquired the assets that they used in that trade from the new owners of the Western Bond?
>
> A. **That is what I found in the revenue agent's report,** yes."
>
> Q. And that is what you are relying upon as the newly discovered matter which you found out?
>
> A. Yes."

But this alleged discovery is irrelevant because it is conceded that the only relevant fact was the value of the assets and **not the source or time of acquisition.** (Tr. p. 160-161).

He testified that the sources from which Farrington got the assets which he traded to the Western Bond for the Western Guaranty stock was **not a proper subject for entry on the books** of the Western Bond, **nor was the time** that elapsed between the acquisition of the assets and their transfer to the Western Bond **a proper matter to set up in the books.** (Tr. p. 165). **He found no changes in the books of the Western Bond with respect to the Western Guaranty transaction.** (Tr. p. 166).

Under his employment in 1936, he was to investigate the transaction relating to the Keystone ranch property:

> "And to see what other items that might be on there that were subject to action by the trustee." (Tr. p. 167).

He checked through most of the transactions of any consequence that pertained to the Bank of California matter, **"I put them aside and did not refer to them, I think, on no occasion until a long time later."** (Tr. p. 167).

He was employed to investigate generally in the original employment. (Tr. p. 168).

In the course of his examinations, he called attention of the plaintiff and his attorney, to other transactions he had looked into. (Tr. p. 175).

If there was no other evidence in the record, the evidence thus far referred to would itself be ample to sustain the findings of fact made by the court below.

It is well settled that corporate books and records and account books to which a party has access, which give notice of the facts, are sufficient to charge interested parties with knowledge which the records would have disclosed and start the running of the Statute of Limitations.

In **Gibson v. Jensen, 158, Pac. 426 (Utah)**, plaintiff's action was barred because he was a stockholder who had access to the corporate books and was found lacking in proper diligence in investigating the books. The court restated the principle that it was **not necessary that plaintiff be informed of all details** and that it was sufficient if she was informed of facts which would put an ordinary person of intelligence and prudence on inquiry.

In **Farmer v. Stendeven, 93 Fed. 2nd, 959, 10th Cir.**, plaintiff was a receiver of a corporation. He sought to recover from its directors and officers, irregular profits on the sales of stock. The court held that the action was barred by the statute of limitations because the records of the stock transfers were reflected in the corporate books; that the receiver was chargeable with notice of what the books of the company reflected and what a reasonably prudent inquiry would have disclosed.

In **Noyes v. Parsons, 177 Pac. 651 (Wash.)**, the suit by receiver was barred, because the receiver had possession of the corporate books and he was held chargeable with knowledge of the facts that could have been derived from the books. The court there

reiterated the principle that the party claiming to have been defrauded must be diligent in making inquiry and that **"means of knowledge are equivalent to knowledge. A clue to the fact which if followed up diligently would lead to a discovery, is in law equivalent to discovery—equivalent to knowledge."**

In **Prentiss v. McWhirtier, supra,** this court held that the claim was barred by the statute of limitations because the plaintiff had access to the corporate records.

Re: Value

There is not a scintilla of evidence in the record to explain why plaintiff could not have investigated in the fall of 1934, the value of the assets which were acquired by Western Bond, in exchange for the Western Guaranty stock. The assets were known. They were specifically identified, and were spread upon the records of the corporation. The value of those assets certainly could have been investigated in 1934 with greater certainty of ascertaining the truth than 15 years after the transaction. The identity of the assets were not concealed. No stumbling block was placed in the way of an investigation, and nothing was done to discourage an investigation.

Plaintiff asserts that the alleged fraud was not discovered until the receipt of the revenue agent's report in 1943. Under this allegation plaintiff had to establish that the revenue agent's report disclosed the facts showing that fraud was committed with

shortly prior to the filing of the bankruptcy petition. It called for investigation at that time. The very nature of the transactions excited attention and inquiry as to why the transactions were carried out and whether the corporation suffered detriment thereby. This at once called for an appraisal of the assets received. At the very time the trustee

reiterated the principle that the party claiming to have been defrauded must be diligent in making inquiry and that **"means of knowledge are equivalent to knowledge. A clue to the fact which if followed up diligently would lead to a discovery, is in law equivalent to discovery—equivalent to knowledge."**

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respect to the value of the assets.

The revenue agent's report, however, does not contain the slightest intimation of fraud in connection with the valuation of the assets received. On the contrary, the revenue agent's report accepts the valuation. They are not questioned. The report recognizes that Western Bond realized a profit of $16,460.23 on the transaction and income tax was paid on that amount by the Western Bond (Appendix p. 9).

Erickson made no discovery of any fact relating to the value of the assets from the report or any other source and he made no appraisal of the assets. (Tr. p. 160). Nothing disclosed by the revenue agent's report caused Erickson or the plaintiff to make any appraisal of those assets, or to make any investigation as to the value.

We submit that there was urgent reason for investigating the value of those assets in 1934. The transaction was an unusual one. It was not a transaction in the ordinary course of business. When the trustee and his attorney and his accountant looked at those records (assuming that they did), they saw an unusual transaction by which a large block of assets were transferred to the Western Guaranty (which was formed for the purpose of receiving from them) in exchange for its stock and that the stock thus obtained was transferred in exchange for other assets. The value of the assets disposed of is alleged to be $322,014.35. The transaction occurred the assets received. At the very time that the trustee

obtained possession of those records he became charged with the duty of examining and investigating that transaction. **That was the incident that set running the statute of limitations** against him, because an investigation at that time into the value of those assets would have disclosed the only material fact that could possibly be the basis of this cause of action.

In **Beal v. Smith**, 189 Pac. 341, (Calif.), a stockholder sued the officers and directors of a corporation to recover from them secret profits which they derived from the transfer of securities owned by the corporation for alleged worthless stock. The court held:

> "The very fact that such a large issue of securities was made in exchange for stock of unknown companies was sufficient to put a prudent man on inquiry."

That is the very situation in the case at bar.

Re: First Revenue Agent's Report

This report is plaintiff's Exhibit 59. It is reproduced so far as material in the Appendix of Exhibits (p. 1-9).

Plaintiff claims in his complaint, contentions in pretrial order and in the evidence in effect that it was the revenue agent's report that opened the vaults that disclosed the alleged fraud and the fraud he discovered was that Farrington acquired the assets which he transferred to Western Bond simultaneously with the transfer of the Western Guaranty stock to

him. (Tr. p. 162). He discovered nothing regarding the **value** of the assets. The report confirmed the valuation at which they were transfered to Western Bond.

The report is dated **October 12, 1932,** and it recites (p. 1) that the information contained in the report was obtained from **"an examination of the books and records of above named affiliated group."** A reading of the report confirms the fact that it purports to show **only what is in the books.**

We submit that plaintiff and his attorneys and his accountants could have obtained the identical information that the revenue agent obtained from the books and records which they had in their possession since the falls of 1934. They could have drawn the same inferences and conclusions as he did.

The facts pertaining to the Western Guaranty stock as narrated by the revenue agent in the report will be found on pages 8 and 9 of the Appendix of Exhibits. That portion of the report discloses the identical information that Erickson said was recorded in the books of the company, except of course, the **conclusions and inferences** that the revenue agent drew therefrom, that the **transactions were simultaneous.** The revenue agent **inferred** that the transactions were simultaneous because the minutes disclosed that on December 20, 1930, Farrington resigned as an officer and director and O'Flynn was elected as officer and director and that at the meeting, after a half hour adjournment a resolution was

adopted authorizing an exchange of the assets. Mr. Gunning in his report does not say that that is actually the fact. He merely says "the understanding apparently being that as soon as the new stockholders came into control of Western Bond", they would cause the company to trade the Western Guaranty stock to Laurel Investment Company for securities previously traded to Farrington. That was the conclusion which he drew from the books and minute entries. The plaintiff, his attorney and his accountant could have drawn the same conclusion. **The significant fact is that the report does not disclose any fact (as distinguished from conclusions) which was not found in the records.**

There is not the slightest intimation in the report that the conclusions were based on any other information than the corporate records.

Instead of disclosing fraud with respect to the only material fact (value), the report confirms the fact that the assets received were of greater value than the assets parted with.

Lack of Diligence in Obtaining Revenue Agent's Report

We submit that the record establishes that plaintiff was lacking in diligence in obtaining the report. Plaintiff knew of its existence when the government filed the claim for additional income tax in 1935. Plaintiff tried to get a copy from the local office of the Internal Revenue Bureau at that time but was

advised they had none. He learned at that time that Mr. Robert T. Jacob, a tax attorney, had a copy. **He waited 3 or 4 years.** Then called at Jacob's office (Tr. p. 119) but did not obtain a copy because Jacob was away and he **never went back to that office again.** (Tr. p. 119). Mr. Teiser obtained a copy from the Internal Revenue Bureau in 1943 for the purpose of contesting the tax claim filed by the government in 1935.

Plaintiff asserts that he did not investigate the tax claim earlier because the referee in bankruptcy (now dead) "stated that there was no reason at that time to contest the claim" because there was no money on hand to pay the claim. But he did not **direct or state** that a copy of the report should not be obtained. He only stated that a contest be deferred.

Getting the report at that time would not have involved any effort or expense. He could have obtained it for the mere asking just as Mr. Teiser did in 1943.

Plaintiff was guilty of gross negligence in waiting from 1935 to 1943 to get a copy of the report. He did not exercise the degree of diligence required in order to prevent the running of the statute of limitations.

That report should have been obtained when its existence became known in order for the trustee to inform himself at least of the losses of the claim. He is charged with the duty **"to examine all proofs of claim and object to the allowance of such claims as may be proper."** (Sec. 47a-8 Bankruptcy Act—11 U.S.C.A. 75a-8). And he should have obtained the report in the performance of his duties to investigate

the affairs of the bankrupt **(Sec. 47a-7 Bankrupt),** for as a lawyer and accountant and from his experience in the Internal Revenue Bureau, he should have known that Internal Revenue reports frequently make disclosures with respect to bankrupts' property which set in motion pursuit of assets.

Re: Consolidated Credit Corporation Stock Transfer

It is alleged (Tr. p. 6) that Farrington fraudulently caused Western Bond to transfer to persons unknown, 40,000 shares of Consolidated Credit Corporation stock which Western Bond owned, in exchange for the capital stock of the Keystone Finance Company, **which Western Bond already owned.**

Plaintiff stated the issues in substantially the same terms in the pretrial order. (Tr. p. 25).

Plaintiff's case establishes that the transaction was spread upon the Western Bond books exactly as alleged in the complaint. Plaintiff's accountant, Erickson, testified (Tr. p. 144) that there is an entry on the books of the Western Bond recording the transaction which recites Western Bond parted with 40,000 shares of the Consolidated stock for which it received 1500 shares of Keystone stock "and the figures are of equal value, for what was parted with and what was received."

Since this entry was in the books in the possession of the plaintiff, he was, of course, chargeable with knowledge of it even if he had not looked at it. But it appears affirmatively from plaintiff's case that

Erickson, the accountant, saw the entry in 1936 (Tr. p. 145-167) in the course of examination of the records, at Mr. Teiser's request who "engaged me to assist him in tracing out the entries on the books." Mr. Teiser had "this matter of **exchange of the Keystone ranch property**" and "to see what other items might be in there that were subject to action by the trustee."

Having found the transaction on the books he "put them aside" and did not refer to them "on any occasion until a long time later." (Tr. p. 167).

He testified he did not discover anything questionable about the transaction. **But the entry itself suggests that the transaction is questionable. The entry records the very fact which plaintiff now complains about, namely—that Western Bond got no consideration because it was already the owner of the Keystone stock** (Tr. p. 6).

Plaintiff himself examined the "main books" of the Western Bond in 1934. (Tr. p. 96). He had the Keystone stock book in 1936. (Tr. p. 131-132).

In 1936, plaintiff commenced the ligitation against the Bank of California to recover the value of the "Keystone" or "Russell" ranch as it is interchangeably referred to, on the grounds that the bankrupt obtained the ranch from Western Bond after the filing of the bankruptcy petition; that Western Bond was the owner of the ranch, although title had been in the Russell Land and Livestock Company, and by it transfered to Keystone Finance Company, because these

two were "wholly owned subsidiaries" of the Western Bond. **Plaintiff so alleged in that proceeding in 1936** (Ex. 103-103a, Appndx. 94-96), and it was **so adjudicated** by Judge Fee (Appndx. 105-108, **44 Fed. Supp. 89**) and by this court **(132 Fed. 2nd, 769).**

This evidence establishes conclusively that plaintiff had knowledge since 1934 and certainly since 1936 of the **very fact which the complaint now charges constituted the fraudulent transaction** and certainly started the running of the statute of limitations.

During the trial, Erickson stated the vice in the transaction in a different way. (Tr. p. 168-169). He said that parties named Tapfer and Snodgrass conveyed title to the Russell ranch in payment for all of the capital stock of the Keystone Finance Co.; that in fact Tapfer and Snodgrass had no title, therefore, Keystone did not acquire the title and hence the transfer of the Keystone stock to Western Bond did not give the Western Bond anything of value; that the title was owned by a man named Russell; that in 1925 he conveyed it to Russell Land and Livestock; that Western Bond owned the stock of the Russell Land and Livestock Company, therefore, Western Bond was already the owner of the ranch by virtue of the stock ownership of the stock of Russell Land and Livestock Company.

The complaint about that transaction is not that the property did not equal or exceed in value the Consolidated Credit Corporation stock but involves

merely the title to the ranch at the time of the transfer. That is the gravamen of that controversy as narrated by Erickson. (Tr. p. 168-169). The only question that presents itself in this respect is whether plaintiff is chargeable with knowledge of those facts and if he did not have actual knowledge whether he could have discovered these facts by the exercise of reasonable diligence more than two years prior to the commencement of this action.

The complaint alleges that the "true character" of the transactions was discovered by the accountant who made an investigation and discovered the facts referred to after the revenue agent's report was obtained.

The testimony of the accountant, Erickson, discloses, however, that the revenue agent's report did not disclose any facts relating to ownership of the ranch. (Tr. p. 184). On the contrary, he said that he obtained this information from

(a) The account books of Western Bond. (Tr. p. 144).

(b) The minute book of Keystone Finance Co. (Tr. p. 148).

(c) The abstract of title. (Tr. p. 148).

The minute book disclosed that Tapfer and Snodgrass paid for their stock by conveying the Russell ranch (Tr. p. 168-169). The abstract of title disclosed that Tapfer and Snodgrass never had any title. (Tr.

p. 169). And the account books disclosed that the Consolidated stock was traded for the Keystone stock.

The accountant testified (Tr. p. 144) that the transfer of the Consolidated Credit Corporation stock in exchange for the Keystone stock was recorded in the books of the Western Bond and and the entries show that the figures are of equal value (the question of value is not involved in this transaction).

He saw the entries when he examined the books in 1936 (Tr. p. 145 and 167) when he was examining into the Bank of California transactions, "I put them aside and did not refer to them, I think, on no occasion until a long time later." (Tr. p. 167).

He testified that he "discovered" from the abstract of title that Tapfer and Snodgrass were never the owners of the property and that therefore Keystone acquired no title by conveyance from them. (Tr. p. 168) and that Russell Land and Livestock Co. was the owner in 1925. (Tr. 168).

At Tr. pp. 183 and 184, his testimony is as follows:

> "Q. Did you or did you not discover the situation in regard to the 40,000 shares of stock, the Consolidated Company stock, at any time prior to 1943?
>
> A. Oh, yes. I saw the record of the transaction, I think, probably in 1936."
>
> . . . . . .
>
> "Q. This minute book of the Keystone Finance Company has been in the files of the Western Bond and Mortgage Company, since you have known anything about those files?
>
> A. I think it was in there in 1936, yes. I am

sure it was.

"Q. **Any investigation of the minutes of the subsidiary corporation would disclose the basis for the stock subscription concerning which you speak?**

A. Yes, sir."

Erickson said he examined the abstract of title in the spring of 1943 in connection with the purchase of the property by a client of his office (Tr. p. 147).

The fact is, however, that the abstract of title was **available for inspection at least since 1936.** At that time, Mr. Teiser had the abstract of title during the trial of the Bank of California case. It was produced during the examination of witness Greene in that proceeding (Exhibit 103, Appendix 109).

Of course, the abstract of title disclosed what was already a matter of **public record** available to all. It is a summary of the instruments affecting the title in so far as they are recorded in the office of the county clerk and recorder. The records are required by law to be kept and everyone is of course, chargeable with at least constuctive notice of those public records.

Where the facts constituting or showing the fraud, appear from the public records required by law to be kept, and open for inspection, plaintiff's ignorance of the fraud will not postpone the operation of the statute of limitations.

37 C.J. 943.
34 Am. Jur. 137.

Section 47(c) Bankruptcy Act—11 U.S.C.A. 75(c) provides:

> "The trustee shall, within ten days after his qualification, record a certified copy of the order approving his bond in the office where conveyances of real estate are recorded in every county where the bankrupt owns real property or an interest therein, not exempt from execution, and pay the fee for such filing."

This mandatory requirement makes it incumbent upon the trustee in bankruptcy as soon as he is appointed, to make diligent inquiry as to the ownership of real property by the bankrupt so that he can perform the function commanded by this statute.

The ownership of the ranch and relationship between Western Bond, Keystone and Russell Companies as of the day of the filing of the petition in bankruptcy was the very foundation of the summary proceedings prosecuted by the plaintiff against the Bank of California. (See proceedings in **McBride v. Bank of Calif., Plaintiff's Ex. 103 and 103A, Appendix p. 95 to 133 and decision by Judge Fee, 44 Fed. Supp. 89 and the decision by this court, 132 Fed. 2nd 769.)**

We submit that the record in that case constitutes ample substantial evidence to support the findings that plaintiff could have discovered the fact as to ownership of the ranch and relationship of the corporations, from sources of information available to him more than two years prior to the commencement of this suit.

We defer discussing the additional evidence at this point because it relates to both transactions and, therefore, will be discussed later.

The very nature of the transaction called for scrutiny. The fact that the corporation parted with an asset of large value alleged to be worth $120,000 (Tr. p. 6 and 7) and that it was exchanged for the stock of the Keystone Company, a corporation which was already owned by the bankrupt, in and of itself at once suggested inquiry as to the bona fides of that transaction (**Beal v. Smith, supra**). Any inquiry into the transaction at that time would have disclosed the very same information which the accountant claims to have discovered in 1943 because he got his information from the account books, minute book and from the abstract.

When the trustee looked at the record of the transaction on the books of the company showing that the Consolidated Credit Corporation stock was transferred in exchange for the Keystone stock (assuming that he did examine that record), he was bound to know at once that there was something wrong for he knew at that time, or so he claimed that the bankrupt already owned the Russell Ranch through the medium of the Russell Land and Livestock Company, and, therefore, the transfer of the Keystone stock was meaningless as consideration. He was then put on notice, or would have been put on notice had he examined the record, which prompted further investigation into the source of title to the Russell ranch.

Judge Fee, who tried this case, also rendered the judgment in the Bank of California case and much weight must be given to his understanding of the issues involved in both cases. He was convinced that the questions tried in the Bank of California case charged the trustee with the duty of further inquiry into the question of the source of title to the Russell ranch and he so indicated in no uncertain terms as is evident from the colloquy between Judge Fee and the accountant Erickson, who claimed to have unearthed the so-called alleged fraud. (Tr. p. 178 to 183).

Judge Fee very properly pointed out to Mr. Erickson during the colloquy (Tr. p. 181):

> "I do not quite see what the purpose of that was, and it is not clear to me what part of this transaction that you are now examining was not clear to you through your investigation of The Bank of California transaction."

But whatever question there might lurk as to when knowledge could have been obtained, was certainly dispelled by Erickson's concluding testimony. (Tr. p. 184). He testified:

> "Q. This minute book of the Keystone Finance Company has been in the files of the Western Bond and Mortgage Co. since you have known anything about those files?
>
> A. I think it was in there in 1936, yes. I am sure it was.
>
> **Q. Any investigation of the minutes of the subsidiary corporation would disclose the basis for the stock subscription concerning which you speak?**
>
> **A. Yes, sir."**

Here is a complete dissipation of the contention that the trustee was without means of knowledge.

Re: Judicial Proceedings in State and Federal Courts

Defendant's Ex. 62, Appndx. p. 16, is a complaint filed in the United States District Court of the State of Oregon, on March 13, 1931, by John Brockie, against Western Bond, Farrington and others.

It alleges that Farrington controlled the Western Bond and many subsidiaries including Western Guaranty, Keystone Finance, and Russell Land and Livestock Co. The complaint specifically charges that Farrington, along with others, misappropriated the Western Guaranty stock. The transaction is described in great detail in Par. IV of that complaint (Appndx. p. 18-20 and thereafter).

The Brockie complaint describes in detail the five items of assets which Farrington transferred to the Western Bond in consideration for the Western Guaranty stock (Appndx. p. 20) and it is there alleged that these assets were worthless (Appndx. p. 20 and 21). This is the very heart of the charge in the case at bar.

The answers interposed by Western Bond (Appndx. p. 33) and Farrington (Appndx. p. 43) put in issue all the material allegations of the complaint and alleged affirmatively that the assets transferred were of equal or greater value than the Guaranty stock. (Appndx. p. 39).

Appellant seeks to avoid the effect of this judicial

record because the suit was dismissed on August 18, 1931. We fail to see any significance in that fact. The entry of the order of dismissal did not expunge the papers from the files. The records were still there to be seen by those who would take the trouble to examine them.

It is important to note, however, that the order of dismissal was entered upon plaintiff's own motion and was "without prejudice." (Appndx. p. 63). The legal implication is that the plaintiff reserved the right to commence another proceeding to enforce the rights asserted in that proceeding. It is not like a judgment entered after a trial on the merits dismissing the complaint, which would carry with it the conclusion that the issues were determined adversely to the plaintiff.

This judicial record charged plaintiff with knowledge of facts which if investigated would have led to the discovery of the facts pertaining to the transaction set forth in the complaint and therefore started the running of the statute of limitations against him.

Ex. 88, Appndx. p. 82, is the complaint filed November 21, 1931, in the Circuit Court of the State of Oregon by H. C. Thompson and others against Western Bond and Mortgage Co.

Ex. 87, Appndx. p. 90, was an order allowing an inspection of the books and records of the Western Bond and Ex. 88, Appndx. p. 92, is the affidavit filed in support of the motion for inspection.

Farrington was not made a party defendant to

that suit. However, the suit was against the Western Bond and in that complaint **Farrington** is charged with the same misconduct as in the Brockie case and in the case at bar, and it deals specifically with the December 20, 1930, transaction. (Appndx. p. 84-86). It alleges that he was in control of the Western Bond and of many subsidiary corporations including the Western Guaranty Co., Keystone Finance Co., Russell Land and Livestock Co., Laurel Investment Company and others.

This judicial record discloses that an order for an inspection of the books and records of the Western Bond was made, but no investigation was made into the facts disclosed by the inspection. The affidavit of Mr. McCurtain, filed in support of that order (Appndx. p. 92), disclosed that he had an audit made of the books and records of Western Bond, but no effort was made to ascertain what that audit disclosed. The complaint and the audit would have led plaintiff to a discovery of the facts pertaining to the transactions referred to in the complaint and that judicial record is sufficient to start running the statute of limitations.

There was another proceeding brought in the State court by Pape and others about the same time in which substantially the same charges were reiterated.

Plaintiff and his counsel knew of those proceedings.

In plaintiff's statement of his contentions in the

pretrial order (Tr. p. 49), he states:

> "**He had a general knowledge that charges had been made and suits or actions brought both in the federal and state courts,** against the Western Bond and Mortgage Company previous to his trusteeship herein in 1934, and that some charges in some of said suits or actions had been made **against C. H. Farrington,** but as to the nature and details of said charges plaintiff was not informed, nor did he have knowledge thereof."

The lack of **knowledge of the details** of the alleged fraud will not prevent the running of the statute of limitations (**37 C.J. 976, Section 359**). Since he had knowledge of the judicial proceedings and that they contained charges against the defendant, it was his duty to examine those proceedings and had he done so, he would have found spread upon those records the very charges which he now asserts in this case. That is particularly true in the **Brockie case** (Appndx. p. 16-26).

Counsel for appellant as a witness in this case testified that he knew of the **Thompson** case and that he talked to Allen McCurtain, attorney for the plaintiff in that case, about it. (Tr. p. 215). The Thompson case was brought into question during the litigation in the Bank of California case (Tr. p. 216), but he did not make any investigation of those complaints (Tr. p. 217).

During the trial of the Bank of California case in 1936, Mr. Teiser questioned the witness Thomas G. Greene about the Brockie case. He knew that Col. Clark was the attorney for the plaintiff in the Brockie

case. (Tr. p. 220). **This was on November 9, 1936** (Tr. p. 220), but the charges made in those proceedings were not investigated.

The plaintiff himself knew of the judicial proceedings. The Assistant Attorney General, Mr. Moody, called Mr. McBride's attention to the newspaper articles that gave a great deal of publicity to the proceedings. (Tr. p. 194). He did that at the very inception of McBride's appointment in the fall of 1934.

Indeed it is not argued in appellant's brief that appellant and his counsel were not aware of the judicial proceedings in the state and federal courts.

Appellant asserts (br. p. 30) "the pleadings in neither of these cases (Thompson and Pape) even remotely referred to the fraud here alleged." The record contradicts that statement. The amended complaint in the Thompson case (Ex. 86, Appndx. p. 82) charges that Farrington was in control of Western Bond and a large number of subsidiary companies, including the Laurel Investment Company, Keystone Finance Company, Russell Land & Livestock Company. He is charged with "juggling the assets" and Par. VII, p. 84, specifically deals with the transaction which took place **December 20, 1930.** It charges the "abstraction" on that date of assets worth $300,000.00 and transfer of those liquid assets to Farrington and Laurel Investment Company (Appndx. p. 86).

With respect to the **Brockie case,** appellant merely argues (p. 30) that if the trustee had examined the records in that case, he would have discovered that

the suit had been dismissed and therefore, as an ordinarily prudent man, he would have ceased further inquiry.

There is, of course, implied in that argument, the admission that he did not examine the records in the Brockie case. Of course, if he had examined the record, he would have discovered not only the order of dismissal "without prejudice", but he also would have discovered the more important fact that Farrington was being charged with fraud in connection with the **very same transaction** (Western Guaranty stock) that is involved in the case at bar. He would have seen that as easily as the order of dismissal. The performance of the plaintiff's duty as trustee demanded that he follow up the charges made in that proceeding and to ascertain the facts pertaining thereto, for it involved the transfer of assets in excess of $300,000.00 **shortly prior to the filing of the petition in bankruptcy.** No effort is made to disclaim knowledge of the existence of the litigations.

In **Pearsall v. Smith, 149 U.S. 231, 13 Sup. Ct. 833,** an assignee in bankruptcy was charged with knowledge of a litigation commenced eleven years before the commencement of the action by the trustee notwithstanding the fact that the trustee only acquired knowledge of that litigation about two months prior to the commencement of his action to set aside fraudulent conveyances. The court said:

> "In the present case the deeds of conveyance by Smith were recorded. **The suit by the Kittels was a public suit."**

In **Lampor v. Osious, 38 Fed. Supp.** 373, the trustee in bankruptcy was charged with knowledge of the judicial records in prior litigations.

In **Bainbridge v. Stoner, 106 Pac. 2nd 423 (Calif.),** the plaintiff was charged with knowledge of the facts disclosed by other judicial proceedings.

In **Feak v. Marion Steamshovel Co., (9th Cir.), 84 Fed.** (2) 670, this court charged the plaintiff with knowledge of facts disclosed by other judicial proceedings involving the same property.

Re: Public Knowledge Through Newspaper Publications

We recognize, of course, that an isolated newspaper account of some occurrence will not charge an ordinary person with knowledge of the transaction. But, that is not true in cases where a great deal of publicity is given to a transaction in newspapers of general circulation.

In this case, the articles were numerous. The attention of the plaintiff was **specifically directed to these newspaper accounts** by Assistant Attorney General Moody immediately after plaintiff's appointment as receiver and subsequent thereto. Mr. Moody arranged that whenever there were any newspaper accounts pertaining to the affairs of the Western Bond that there were to be clipped and turned over to him and he in turn relayed them to the plaintiff (Tr. pp. 194-199). There is a large folder full of newspaper clippings in evidence (Paintiff's Ex. p. 162, Tr. p. 266).

We have printed excerpts from a number of these newspaper clippings (Appendx, pp. 30, 31, 32, 64, 66, 69, 71, 74, 76, 77, 78, 80, 81). They are replete with reference to the court proceedings charging fraud against Farrington. As for example (Ex. 64, Appendx. p. 31), the article dated March 13, 1931, recites that in the Brockie suit it is charged that Farrington through an intricate network of dummy companies abstracted more than $300,000.00 worth of assets of the firm.

Ex. 75, Appndx. p. 64, recites the filing of the Thompson suit and that it is charged therein that Farrington and O'Flynn and others entered into a conspiracy to abstract assets in the sum upwards of $300,000.00. To the same effect are all the newspaper articles introduced in evidence. Plaintiff's counsel had the whole sheaf of newspaper articles in his possession in the Bank of California case in 1936, and he examined the witnesses in reference to those articles. (Tr. pp. 225 to 239). He examined Thomas G. Greene particularly in reference to the credit file (Ex. 162) which contains a great many of the articles (Tr. p. 230 to 237).

It is highly significant that in 1936, Mr. Teiser attempted to charge Thomas G. Greene, attorney for the Bank of California, with knowledge of the facts conveyed by these newspaper articles, but now, counsel insists that they conveyed no notice to him or to the plaintiff.

We submit that the articles were so numerous and

were of such a character that they charged plaintiff with knowledge of all the facts that would have been discovered had he investigated the charges made therein. This was particularly his duty because Mr. Moody had specifically called it to his attention for that very purpose. These articles, therefore, started the running of the statute of limitations.

General public information has been held sufficient to charge a litigant with notice and start the running of the statute of limitations.

In **Stone v. Winn, 176 S.W. 933,** a taxpayer sued for an injunction to enjoin the fiscal court from levying a tax to pay bonds that had been previously issued. The suit was predicated on fraud in the election which approved the bonds. The Kentucky court held that the suit was barred by the statute of limitations since the claim of fraud was a matter of **public information** in that county which started the running of the statute.

Information Imparted to Plaintiff by Assistant Attorney General Moody

The record discloses as soon as plaintiff was appointed receiver, Mr. Ralph Moody, Assistant Attorney General of the State of Oregon, called on plaintiff and informed him of the prior investigations made by the office of the Attorney General and the Corporation Commissioner; of the great concern that they had over the disposition of the assets of the corporation, and that Farrington was being accused of the unlawful transfer of assets. Mr. Moody called plain-

tiff's attention to the newspaper accounts of several litigations in which charges of fraud were made against Farrington and urged an extensive investigation into the civil and criminal liability of Farrington and all others who might be responsible.

We submit that this information coming from a high state official, coupled with the duties the Bankruptcy Act itself imposed upon plaintiff, was sufficient to charge plaintiff with the realization of the gravity of the situation and required more than ordinary diligence and scrutiny in investigating the affairs of the corporation. This information made it absolutely necessary for plaintiff to investigate at least the **major transactions** resulting in the transfer of assets **within a short period of time prior to the filing of the Petition in Bankruptcy** which would have included the two transactions involved in this case. One took place less than two years prior to the filing of the Bankruptcy Petition and the other less than one year prior thereto. These two transactions resulted in a transfer of assets alleged to be a total of over $440,000 and certainly were large enough and of sufficient importance to challenge attention and scrutiny and fullest investigation into (a) the value of the assets received in exchange therefor, and (b) any other factors affecting the good faith of the transaction. We say, therefore, that the information imparted to plaintiff by the Assistant Attorney General was a fact potent to start running the statute of limitations, for so grave was his concern and so insistent was he upon a thorough investigation that they provided for

the payment of a salary by the State of Oregon to the receiver as well as supplying him with office space and office expense, a most unusual procedure.

Re: Concealed, Camouflaged, Misleading and False Entries on the Books

The complaint attributes delay in discovering the alleged fraud to concealed, camouflaged, misleading and false entries on the books of Western Bond and Mortgage Co. (Tr. p. 7).

We submit that there is not a scintilla of evidence in the record to sustain this allegation. Appellant does not in his brief point to a single item of evidence in support of the allegation. **There is no such finding of fact.** On the contrary, the accountant, Erickson, testified that Western Guaranty transaction was spread upon the records and he does not point to a single false entry in connection therewith. The records disclosed the transfer of assets from Western Bond to Western Guaranty in exchange for its stock, the transfer of the Western Guaranty stock to Farrington, and the consideration received therefor. The valuation placed upon the assets was also recorded in the minutes of the board of directors by the resolution that the value of the assets received were equal to or greater than the assets transferred. The only entries which plaintiff claims are not recorded in the books are:

(a) The source from which Farrington obtained the assets which he transferred in consideration for Western Guaranty Stock.

(b) The time that elapsed between their acquisition and the transfer to Western Bond.

As to these facts the accountant, Erickson, testified that they do not properly belong upon the books of the Western Bond. (Tr. p. 165). That is obviously so because those two facts relate to the transaction between Farrington and O'Flynn, inter se, **They do not relate to a transaction to which Western Bond was a party.**

The transfer of the Consolidated Corporation stock was likewise spread upon the records of the Western Bond. There is not a word of evidence of the concealment of any fact in relation to that transaction. As far as the Western Bond was concerned the transaction consisted of the transfer by it of the Consolidated stock and the receipt by it of the Keystone stock. These entries were recorded.

Here to, appellant's brief does not point to a single item of evidence of any thing that should have been recorded which was omitted. Neither does it point to any entry in the books that is erroneous in this respect much less false.

Re: Lack of Funds to Finance Investigation

Appellant attempts to excuse the failure to investigate the affairs of this corporation and particularly the alleged frauds charged in the complaint by the repeated assertions that the estate did not have much money and that the small amount of money was earmarked for investigation and prosecution of

the Bank of California suit. (appellant's brief p. 26 and 27). We know of no reason why funds should be earmarked for the investigation of one transaction any more than another.

In any event, it is settled beyond question that the lack of funds or even poverty which prevents investigation will not prevent the running of the statute of limitations.

Leggett v. Standard Oil Company, 149 U.S. 287.
Cummings v. Wilson & Willard Mfg. Co., 4 Fed. 2nd 453, 9th Cir.
Gillons v. Shell Co., 86 Fed. 2nd, 600, 9th Cir.
Baillie v. Columbia Gold Mining Co., 86 Ore. 1-22.

Lack of funds did not account for the failure to investigate, because plaintiff was given the services of two expert auditors from the Oregon Corporation Department without limit, he was paid a salary of $150.00 per month and office expense by the state, and from the middle of 1936 he had the services of the certified pubic accountant who agreed to render his services on a contingent basis to investigate all matters.

Moreover, no expense was needed to discover the pertinent facts. The Western Guaranty stock transaction only involved the question of the value of the assets received which were spread on the books and the Consolidated Credit Corporation stock involved the ownership of the Russell ranch which was ascertainable from the abstract of title.

Re: Knowledge Obtained by Counsel for Plaintiff

Plaintiff was chargeable with knowledge of all the facts or information which was obtained or came into the possession of his counsel, Mr. Latourette and Mr. Teiser.

It is a well recognized rule that knowledge of facts relating to the subject matter of the employment acquired by an attorney while he is engaged in the discharge of his duties under the employment is imputed to his client. (See cases annotated—**4 A.L.R., 1594** and **38 A.L.R. 820**. The same rule is set further in **5 Am. Jur. p. 302, section 74.)**

CONCLUSION

We submit that judgment appealed from should be affirmed because:

(a) Appellant's Specification of Errors do not raise any issue with respect to the sufficiency of evidence to sustain the findings of fact upon the issue of laches and if that contention be sustained all other questions become moot.

(b) Assuming without admitting that the issue of laches is properly before the court for review, the record establishes that there is a great abundance of evidence to sustain the findings of fact upon which the court below applied the doctrine of laches.

If the court holds that the suit is barred by laches, the question of the application of the statute of limitations becomes moot.

(c) There is an abundance of evidence to sustain the findings of fact of the court below upon which it made its determination that the action was barred by the statute of limitations.

Respectfully submitted,

S. J. BISCHOFF,
Attorney for Appellee.